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BEFORE THE ARIZONA CORPORATION COMMISSION 28

**COMMISSIONERS**

JEFF HATCH-MILLER – Chairman FEB 23 P 3: 42

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AZ CORP COMMISSION  
DOCUMENT CONTROL

ARIZONA WATER COMPANY, an Arizona  
corporation,

Complainant,

vs.

GLOBAL WATER RESOURCES, LLC, a foreign  
limited liability company; GLOBAL WATER  
RESOURCES, INC., a Delaware corporation;  
GLOBAL WATER MANAGEMENT, LLC, a  
foreign limited liability company; SANTA CRUZ  
WATER COMPANY, LLC, an Arizona limited  
liability corporation; PALO VERDE UTILITIES  
COMPANY, LLC, an Arizona limited liability  
corporation; GLOBAL WATER – SANTA CRUZ  
WATER COMPANY, an Arizona corporation;  
GLOBAL WATER – PALO VERDE UTILITIES  
COMPANY, an Arizona corporation; JOHN AND  
JANE DOES 1-20; ABC ENTITIES I – XX,

Respondents.

DOCKET NO. W-01445A-06-0200  
SW-20445A-06-0200  
W-20446A-06-0200  
W-03576A-06-0200  
SW-03575A-06-0200

**REPLY TO  
STAFF'S BRIEF**

Arizona Corporation Commission  
**DOCKETED**

**FEB 23 2007**

DOCKETED BY

NR

Santa Cruz Water Company, LLC; Palo Verde Utilities Company, LLC; Global Water –  
Santa Cruz Water Company; Global Water – Palo Verde Utilities Company; Cave Creek Water  
Company; and Hassayampa Utility Company (the “Global Utilities”) and Global Water Resources,  
LLC (“Global Parent”)(collectively “Global”) hereby provide their reply to the Brief filed by Staff  
on February 9, 2007 in this docket.

1     **I. Preliminary Statement.**

2             Global agrees with much of what Staff said in its brief. In particular, Staff properly noted  
3     that Infrastructure Coordination and Financing Agreements ("ICFAs") serve many goals – such as  
4     water conservation and consolidation of weak utilities – that serve the public interest. Further,  
5     Staff was correct to conclude that this is the not the right time to decide jurisdictional questions  
6     regarding Global Parent and other unregulated Global affiliates (collectively, the "Unregulated  
7     Affiliates"). Staff was also right to observe that piercing the corporate veil is very difficult.

8             Global agrees with Staff that, given the undeveloped state of the record, this is not the right  
9     time to reach firm conclusions or final decisions on jurisdictional or other questions. However, to  
10    the extent that the Commission desires to address these issues at this time, there are no grounds to  
11    find that any of the Unregulated Affiliates are public service corporations. First, only entities that  
12    provide the services specified in the Arizona Constitution may be determined to be public service  
13    corporations. The Unregulated Affiliates do not provide water, wastewater, or any of the other  
14    specified services. Second, there are no grounds in the record for a finding of undercapitalization,  
15    fraud, or misconduct, and thus the separate corporate existence of the Unregulated Affiliates may  
16    not be disregarded. Third, so called "*Serv-Yu*" factors<sup>1</sup> do not support a finding that the Global  
17    Parent are public service corporations because they only provide non-utility service under private  
18    contract, with all utility services provided by the fully regulated Global Utilities. Thus, the time is  
19    not right to decide these issues, but if a decision is made now, there are no grounds for declaring  
20    the Unregulated Affiliates to be public service corporations.

21    **II. It is not prudent to make a decision at this time.**

22             Staff's Brief repeatedly notes the limited state of the record at this time. For example, Staff  
23    noted that the jurisdiction issue "is not clear at this point."<sup>2</sup> Likewise, Staff noted that "absent a  
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26    <sup>1</sup> See *Natural Gas Service Co. v. Serv-Yu Co-Op.*, 70 Ariz. 235, 237-38, 219 P.2d 324, 325-36  
27    (1950).

<sup>2</sup> Staff Brief at 2.

1 more developed record... it is impossible to determine at this point with certainty” whether the  
2 Commission should take jurisdiction.<sup>3</sup>

3 Likewise, the Staff Report in the Generic Financing Docket<sup>4</sup> did not make any firm  
4 conclusions regarding ICFAs. Staff described its report as only a “preliminary evaluation”<sup>5</sup> and its  
5 suggestions as only “preliminary positions”<sup>6</sup> Further, the Director of the Utilities Division, Mr.  
6 Johnson, recently referred to the Staff Report as a mere “position paper” and encouraged the  
7 Commission to obtain further information.<sup>7</sup> Thus, it is clear that Staff’s analysis of the ICFAs is  
8 only tentative at this point.

9 It would not be prudent to base a final decision on incomplete, tentative analysis by Staff.  
10 Further, it is clear that the record will become much more developed in the future. It is our  
11 understanding that once this briefing schedule is complete, the Commission will request further  
12 rounds of comments in the Generic Financing Docket. In addition, there may be workshops or  
13 other information gathering sessions. Thus, the record will likely be further developed in the  
14 future. Therefore, Staff was correct to reserve judgment until all the facts are in. The Commission  
15 should follow the same course.

16 In addition, it should be noted that the Staff did not make a clear finding that ICFA fees  
17 should be treated as advances or contributions. As described above, Staff’s conclusions were only  
18 tentative. Moreover, the relevant section of the Staff Report did not directly examine the ICFAs.  
19 Rather, this section analyzed a hypothetical only loosely based on the ICFAs.<sup>8</sup> This hypothetical,  
20 called “Scenario 3” differs from ICFAs in several important respects. For example, Scenario 3  
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23 <sup>3</sup> Staff Brief at 10-11.

24 <sup>4</sup> Docket No. W-00000C-06-0149.

25 <sup>5</sup> Generic Financing Docket, Staff Report at 2.

26 <sup>6</sup> Generic Financing Docket, Staff Report at 4.

27 <sup>7</sup> Comments made during the Commission’s Staff Meeting on January 17, 2007.

<sup>8</sup> Generic Financing Docket, Staff Report at 5-6

1 involves "services typically covered by 'off-site hook-up fees'". Our Comments in the Generic  
2 Financing Docket explained why the ICFA fees are substantially different from hook-up fees.

3 There are many other differences between ICFA fees and advances or contributions. For  
4 example, Global Parent pays taxes on the ICFA fees, while advances and contributions to water  
5 and wastewater companies are tax-free. In addition, ICFA fees only cover an approximation of the  
6 carrying costs of the plant – they do not directly pay for the plant, as suggested in Scenario 3.  
7 Moreover, ICFA fees are often used to pay for the acquisition and consolidation of small utilities,  
8 which does not impact rate base at all. Staff also notes that over-reliance on advances and  
9 contributions leads to undercapitalization and financially weak utilities.<sup>9</sup> It thus makes little sense  
10 to treat new alternatives to advances and contributions as being advances and contributions.

11 Most importantly, hook-up fees, and other financing methods that result in advances or  
12 contributions, simply do not result in regionally sized, conservation-focused infrastructure, such as  
13 reclaimed water facilities, use of surface water, and construction of recharge wells. Such facilities  
14 are enormously capital intensive. It is therefore necessary for there to be a mechanism for  
15 investors to recover the carrying costs of these massive investments until they go into service.

16 Further, traditional methods do not result in consolidation of utilities. Tellingly, American  
17 Water (parent of Arizona-American) aims for between 20 and 30 acquisitions per year – yet it has  
18 not acquired any utility in Arizona in years.<sup>10</sup> Other publicly traded water companies also pursue  
19 acquisitions, but they avoid Arizona because Arizona's traditional financing methods simply don't  
20 support consolidation. Yet with more than 400 water companies and explosive growth in the state,  
21 there is a desperate need for such consolidation. The ICFA presents a new alternative that can  
22 partially fund consolidation activity. The Commission should not squash such a promising new  
23 alternative. And to be clear, Global does not claim exclusive rights to the ICFA model. Indeed,  
24 Global encourages other sophisticated companies with access to capital to adopt this method and  
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27 <sup>9</sup> Generic Financing Docket, Staff Report at 6.

<sup>10</sup> "Water for Profit", [www.cfo.com](http://www.cfo.com), dated February 1, 2007.

1 provide the necessary capital to consolidate Arizona's small, fragmented utilities and to build the  
2 massive amounts of conservation-based infrastructure that will be needed to sustain growth – the  
3 engine of our state's economy.

4 Thus, ICFA's are clearly in the public interest. Staff correctly concluded that "ICFA type  
5 arrangements can provide appropriate long-term solutions which promote conservation of water  
6 supplies and efficient wastewater utilization."<sup>11</sup> Staff was thus right to conclude that ICFA type  
7 agreements should be reviewed "on a case by case basis."<sup>12</sup> Given the undeveloped state of the  
8 record, and the clear benefits of ICFA's, it is not prudent at this time to make blanket  
9 determinations regarding whether ICFA fees should be advances, or whether ICFA signatories are  
10 public service corporations.

11 **III. The Unregulated Affiliates are not public service corporations.**

12 For the reasons described above, this is not the time to decide these questions. But if the  
13 Commission wishes to push ahead with a decision at this time, there are no grounds to find the  
14 Unregulated Affiliates to be public service corporations. First and foremost, the Unregulated  
15 Affiliates simply do not provide water, wastewater, or any other service listed in the Article XV §  
16 2 of the Arizona Constitution. There is simply no reference in Article XV to coordination or  
17 financing services. Staff appropriately quotes the language of the key case: "we simply note that  
18 the constitutional definition is to be strictly construed and that [the holding company] itself does  
19 not provide any public service listed in the definition." *Arizona Public Service Co. v. Arizona*  
20 *Corp. Comm'n*, 155 Ariz. 263, 267, 746 P.2d 4, 8 (App. 1987) *affirmed in relevant part, vacated*  
21 *in part on other grounds*, 157 Ariz. 532, 760 P.2d 532 (1988). A corporation which does not  
22 provide the listed services cannot be a public service corporation – that is simply the end of the  
23 matter. The text of the constitution permits no other result.

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27 <sup>11</sup> Generic Financing Docket, Staff Report at 7.

<sup>12</sup> *Id.*

1 This conclusion is reinforced by the most recent case concerning public service  
2 corporations. Only months ago, the Court of Appeals noted that “[d]etermining whether an entity  
3 is a public service corporation requires a two-step process. First, we considered whether the entity  
4 satisfies the literal and textual definition of a public service corporation under Article 15, Section 2  
5 of the Arizona Constitution.” *Southwest Transmission Co-op. v. Arizona Corp. Comm’n*, 213  
6 Ariz. 427, 142 P.3d 1240, 1243 ¶ 16 (App. 2006) citing *Southwest Gas Corp. v. Arizona Corp.*  
7 *Comm’n*, 169 Ariz. 279, 285-86, 818 P.2d 714, 720-21 (App. 1991). If – and only if – step one  
8 produces an affirmative result, can the decision-maker move on to step 2 (the so-called “*Serv-Yu*”)  
9 factors. See *id.* No party contends that the Unregulated Affiliates meet the “literal and textual  
10 definition”, so the Unregulated Affiliates cannot be public service corporations.

11 Staff suggests that the Commission could engage in an “alter ego” or “veil piercing” type  
12 of analysis. However, as noted above, if an entity does not meet the “literal and textual definition”  
13 it cannot be considered a public service corporation. But in any event, Staff correctly notes that it  
14 is very difficult to pierce the corporate veil, explaining that “absent some fraud or injustice, Courts  
15 are hesitant to simply ignore the corporate separation.”<sup>13</sup> The case most directly on point is  
16 *Arizona Public Service, supra*. That case involved the holding company of APS. The  
17 Commission argued that the court should disregard the separate corporate existence of the holding  
18 company. The court rejected that argument, noting that “[w]e decline to “pierce the corporate  
19 veil” because both [the holding company] and APS have maintained their separate corporate  
20 identities and because the Commission has offered no evidenced of undercapitalization, fraud,  
21 misconduct, or impropriety in the management or operation of the two companies.” *Arizona*  
22 *Public Service*, 155 Ariz. at 267, 746 P.2d at 8. The Unregulated Affiliates have maintained their  
23 formal, separate identities, the regulated Global Utilities are highly capitalized, and no party has  
24 clearly identified any “fraud or injustice.” Thus, Staff correctly concludes that “absent a more  
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<sup>13</sup> Staff Brief at 7.

1 developed record on such injustices or misconduct, it is impossible to determine at this point with  
2 certainty whether piercing of the corporate veil is appropriate.”<sup>14</sup>

3 In addition, the Commission “is without jurisdiction to compel” an entity to “submit to its  
4 control” when the entity has not been previously regulated and does not consent to the  
5 Commission making the jurisdictional finding. *See Williams v. Arizona Corp. Comm’n*, 102 Ariz.  
6 382, 430 P.2d 144 (1967). Instead, such determinations must be made in the courts.

7 **IV. The Serv-Yu factors do not support finding of jurisdiction.**

8 As noted above, the *Serv-Yu* factors do not apply because the Unregulated Affiliates do not  
9 meet the “literal and textual” definition in Article XV § 2. In addition, the Commission lacks  
10 jurisdiction to decide the issue under *Williams*. However, because Staff addressed the *Serv-Yu*  
11 factors, we will briefly address each factor. Staff only addressed Global Parent, so this discussion  
12 will involve only Global Parent.

13 **A. Factor One.**

14 The first factor is “what the corporation actually does”. Global Parent provides  
15 coordination and financing services under the ICFAs. It also consolidates regulated utilities and  
16 invests equity to fund infrastructure needs, including needed conservation infrastructure for  
17 reclaimed water, surface water, and recharged water. Global Parent does not provide water,  
18 wastewater or reclaimed water service. The ICFAs carefully limit the role of Global Parent to non-  
19 regulated functions. The regulated Global Utilities provide the water, wastewater, and reclaimed  
20 water services. No water, wastewater, or reclaimed water customer will ever receive a bill from or  
21 payable to Global Parent. The regulated Global Utilities remain subject to the CC&N process and  
22 resulting conditions. Further, they enter into main extension agreements for on-site facilities in  
23 accordance with Commission rules. Thus, this factor points against jurisdiction over Global  
24 Parent.

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<sup>14</sup> *Id.* at 10-11.

1           **B.      Factor Two.**

2           The second factor is dedication to public use. To meet this factor, the entity “must at least  
3 have undertaken to actually engage in business and supply at least some of his commodity to some  
4 of the public.”<sup>15</sup> Here, Global Parent does not supply the relevant commodity – water. And  
5 Global Parent does not deal with the general public – only developers and other large landowners.  
6 Thus, this factor points against a finding of jurisdiction.

7           **C.      Factor Three.**

8           The third factor is “articles of incorporation”. No provision in Global Parent’s articles  
9 suggests that it is a public service corporation.

10          **D.      Factor Four.**

11          The fourth factor is dealing with the service of a commodity in which the public has been  
12 generally held to have an interest. Again, Global Parent does not deliver a drop of water. Only the  
13 regulated utilities provide this service. Unlike *Southwest Transmission*, here Global Parent never  
14 takes ownership or possession of the relevant commodity. Thus, this factor points against a  
15 finding of jurisdiction.

16          **E.      Factor Five.**

17          The fifth factor is “monopolizing or intending to monopolize the territory with a public  
18 service commodity.” *Serv-Yu*, 70 Ariz. at 238, 219 P.2d at 326. Again, Global Parent does not  
19 provide a public service commodity. And there is no intent to monopolize. A monopoly is only  
20 created – for the regulated utility – when the Commission grants a CC&N. The ICFA’s expressly  
21 provide that if the Commission denies the CC&N, the landowner is free to terminate the ICFA.  
22 Thus, this factor also points against jurisdiction.

23          **F.      Factor Six.**

24          The sixth factor is acceptance of “substantially all requests for service.” Here, Global  
25 Parent does not provide water, wastewater, or reclaimed water service. And even if the ICFA’s are  
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<sup>15</sup> Staff Brief at 9 citing *Serv-Yu*.



1 considered a relevant service, there is no evidence in the record that Global Parent accepts all  
2 requests for ICFAs. Thus, this factor points against jurisdiction.

3 **G. Factor Seven.**

4 Service under private contract points against jurisdiction, although this factor is not  
5 controlling. Again, Global Parent does not provide the relevant service. And in any event, the  
6 services it does provide are provided pursuant to private contracts (the ICFAs), so this factor  
7 points against jurisdiction.

8 **H. Factor Eight.**

9 The eighth and last factor is competition with other public service corporations. Staff notes  
10 that the "Coordinator and its operating affiliate[s] would together meet this criteria."<sup>16</sup> But  
11 because there are no grounds to pierce the corporate veil, the companies must be analyzed  
12 separately. Global Parent does not compete directly with regulated utilities, although its regulated  
13 subsidiaries, the Global Utilities certainly do. Because these are separate entities, this factor points  
14 against jurisdiction.

15 **I. Conclusion**

16 No factor points in favor of jurisdiction, so a public service corporation finding is clearly  
17 not warranted under the *Serv-Yu* factors, even if those factors could be applied in these  
18 circumstances.

19 **V. Jurisdiction over agreements.**

20 Staff also suggests that even if the Global Parent are not public service corporations, the  
21 Commission can still assert jurisdiction over the ICFAs. It is not clear what Staff means by this  
22 suggestion. They cite to *Woods*, the case that affirmed the Commission's Affiliated Interest Rules,  
23 A.A.C. R14-2-801 et seq. Santa Cruz Water Company recently became a "Class A" utility, so  
24 Global Parent is now subject to these rules. However, Staff does not point to any provision of  
25 those rules that apply here, and there does not appear to be any provision in the rules that apply to  
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<sup>16</sup> Staff Brief at 12.

1 the ICFAs. The rules do require approval for agreements where the utility guarantees the obligations  
2 of an affiliate. A.A.C. R14-2-804(A)(1). The ICFAs involve no such guarantee – instead they  
3 involve the opposite – as Global Parent guarantees the obligations of the regulated utilities. It  
4 seems likely that the Commission would want to encourage parent companies to stand behind  
5 utilities in this way.

6 Staff may have been referring to its recommendation in the Staff Report that ICFAs be  
7 evaluated on a “case by case” basis in appropriate proceedings. Global fully agrees with that  
8 suggestion. The Commission certainly has the power to investigate the effect of ICFAs on rates in  
9 the context of a rate case. A rate case proceeding would supply a lot of the information that is  
10 missing from this record. And because the Commission clearly has jurisdiction over the rates of  
11 the Global Utilities, such an approach would provide a much firmer basis for the Commission to  
12 act. Global recently suggested that the Commission order several of the Global Utilities to file rate  
13 cases.<sup>17</sup>

14 **VI. Conclusion.**

15 Given the limited development of the record at this point, this is not the right time to  
16 decide the jurisdiction question. But if a decision is made, the Unregulated Affiliates are not  
17 public service corporations for several reasons – they do not meet the textual definition, there are  
18 no grounds for piercing the corporate veil, the *Serv-Yu* factors (even if applicable) do not support  
19 jurisdiction, and in any event, under *Williams*, the Commission may not assert jurisdiction under  
20 these circumstances.

21 Thus, the Commission should not make a jurisdictional finding at this time. The  
22 Commission would be on much firmer footing in evaluating the effects of ICFAs on rates in future  
23 rate cases for Global Utilities.

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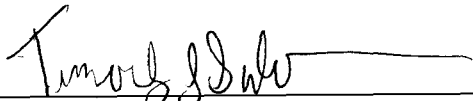
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<sup>17</sup> See Rebuttal Testimony of Cindy Liles at pages 20-21 in Docket No. W-01445A-06-0199 et al.

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1 RESPECTFULLY SUBMITTED this 23<sup>rd</sup> day of February 2007.

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